

Extract: Transport Select Committee - Eighth Report - Search and Rescue

April 2005

VAT

53. We also heard concerns from the RNLI, Mountain Rescue—England and Wales and ALSAR about their liability for VAT on equipment. Ms Margaret Bennett, Secretary of ALSAR told us that she and lowland search staff would

"feel a bit more appreciated if we were given some of the VAT benefits which are available to other types of charities and are not available to us. Even in regard to search and rescue I know that sea rescue charities have a far greater range of products which they buy which are VAT exempt, or zero rated."[\[104\]](#)

54. The RNLI incurred additional costs of £3.9m in 2003 through the payment of irrecoverable VAT. [\[105\]](#) Mr Freemantle told us that this was the price of two all-weather lifeboats.[\[106\]](#)

55. The Government is not willing to allow all voluntary organisations to recover the VAT they pay, nor is it willing to differentiate between voluntary organisations in order to reimburse some of them. The Government told us that:

"For more than two decades, charities have been pressing successive governments to change the rules to reduce or reimburse them for their irrecoverable VAT bills, and no Government has considered the issue more seriously than this one. Twice, in the 1999 Treasury Review of Charity Taxation, and in the 2002 Cross Cutting Review of The Role of the Voluntary and Community Sector in Service Delivery, we have conducted major reviews to see if we could find an efficient, affordable, principled solution to the problem of irrecoverable VAT.

"Through these reviews, we came to two conclusions: first, that it would not be an affordable or efficient use of public resources to reimburse all 250,000 charitable bodies in the UK for the VAT they incur, regardless of the activities they are involved in or their financial health, and which would cost between £500 million and £1 billion per year; and second, that there was no fair and principled basis on which we could decide that some charities would be reimbursed their VAT and some would not. (...)

"It is a fundamental principle of VAT that tax incurred on purchases can only be recovered by VAT registered bodies if it relates to taxable business activities. This means that charities providing services for no charge, or providing services which are exempt from VAT, cannot recover the VAT they incur on purchases related to these services."[\[107\]](#)

56. The Government needs to use this statement with care: it could be seen as incitement to the SAR voluntary organisations to charge the Government for their services. The Government also told us that each year it provided voluntary organisations with over £200m in *relief* from VAT (which we understand to mean that VAT on the goods and services provided by certain voluntary organisations was charged at a level lower than the standard rate), and that "[t]his forms part of the total Government funding for the voluntary and community sector, which stands at £3.3 billion per year."[\[108\]](#) The suggestion that income foregone by the Exchequer constitutes "funding for the voluntary and community sector" involves an unusual definition of "funding", but, as we set out below, we are more concerned that while the Government's position on VAT is unshakeable, the alternative routes it suggests voluntary organisations should use to maximise their income are of limited use to the RNLI, which pays £3.9m VAT each year.

57. Ms Mactaggart told us that, in discussions with the Treasury,

"the conclusion has been that the most effective way to increase the income of a voluntary organisation, like the RNLI, which depends on donations, is through very substantial tax breaks on charitable giving and effective encouragement of tax-efficient giving, which can increase the value of donations by 33 per cent. We are focusing on the income to be dealt with by tax breaks rather than on the expenditure."[\[109\]](#)

58. Tax-efficient giving, such as Gift Aid, can undoubtedly increase the benefit charities derive from donations from UK taxpayers. Nevertheless, it is misleading for the Government to simply shift the focus from irrecoverable VAT to tax-efficient giving for two reasons: first, because the combined effect of greater use of tax-efficient charitable giving and VAT refunds would be greater than the effect of tax-efficient charitable giving alone; and second, because legacies left to charities are already tax-efficient (because they are exempt from inheritance tax). As recorded above, 68% of the RNLI's fundraising income came from legacies in 2003.

Conclusion and recommendation

59. Encouraging tax-efficient donations is insufficient on its own to help SAR voluntary organisations make the most of the money they receive; the RNLI receives most of its income from legacies, which are already tax-efficient. The Government must reconsider whether voluntary SAR organisations should be relieved of the burden of their VAT payments in some way. We suggest that they should; the service they provide could not be foregone because of the UK's international obligations; it would have to be financed by the state if it was not funded by donations. It is not surprising that SAR voluntary organisations feel under-valued by Government: they provide essential services cheaply, but a significant proportion of their fundraising effort services the Exchequer. If there is a legal problem which prevents the *recovery* of VAT, the voluntary organisations could receive an annual grant to off-set their VAT payments over the previous year; the precise method is less important than the effect.

Government response

The Government has made clear that we will work with charities to improve the VAT system where possible, but, for the reasons given to the Select Committee and quoted in its report, we do not agree that a funding scheme for charities based on irrecoverable VAT is a practical or affordable way of targeting the Government support available for charities.